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## AN OVERVIEW OF THE VIRGINIA UCITA

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### AN OVERVIEW OF THE VIRGINIA UCITA Presentation to Symposium The University of Richmond School of Law March 2, 2001

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{1} Virginia has taken a strong and important leadership in establishing rules for the Information Highway through the Joint Committee on Technology and Science (JCOTS) and Delegate Joe T. May. Without the Uniform Computer Information Transactions Act (UCITA) no established rules exist in common law for the Information Highway, which means that each judge must create the rules in each case as it arises. Every judge will make his own rules for the particular case. This results in great inconsistency and uncertainty adversely affecting the realization of the full potential of the Information Age economy. Governor Gilmore states:

In 2000, Virginia was the first state to enact UCITA, and I was proud to be the first governor in the nation to sign it into law. We did so with the expectation that a sound legal structure would attract entrepreneurs to locate in Virginia, generate prosperity here, and enhance our quality of life.<sup>[1]</sup>

{2} It is inconceivable that an electronic signature or an electronic contract, or term thereof, should be valid in Virginia but not in California, or indeed, in the U.S. but not in the U.K. or France.

{3} The Internet is borderless and faceless. E-Commerce is driving our economy and enhancing productivity and economic growth. Not very long ago, we transacted business face-to-face. Now we do business where and whenever we choose. On every airline flight, laptop computers are open and contracts are being made while flying over an unknown state with a party at an unknown location. Has a valid contract been entered into? With whom? Did the party have authority to contract? What are the terms of the contract? Can the contract be attributed to a particular person? What law governs? What forum has jurisdiction? All these questions need answers.

#### SNAPSHOT OF UCITA

{4} Like the Uniform Commercial Code (UCC), enacted in all states, UCITA's principal theme is that innovation and competition is best fostered in a free market, where the parties may choose the technology and business models that best suit their transaction. The outline of UCITA parallels UCC Article 2 for sale of goods:

Gap-filler rules Two-thirds of UCC Article 2 and of UCITA's 106 sections are default rules that come into play only if the express terms of the agreement of the parties are silent on a matter and a term cannot be supplied by trade usage, course of dealing, or past performance of the parties.<sup>[2]</sup>

Only when the Agreement is silent, and trade usage, etc., does not fill the gap do the default rules of UCITA fill the gap. In the event the default rules (based upon general business practice) are not appropriate for the particular transaction, the parties may include an express term that is appropriate. With the exception of only a few default rule sections, there is no controversy over the approximately

Formation Rules UCITA expands the contract formation rules to encompass electronic contracting for information. These rules comprise about 20% of UCITA's sections. They follow the wording and provisions of the new E-Signature federal act and Uniform Electronic Transactions Act (UETA), which, if enacted by a state, lifts the federal preemption. In addition, UCITA provides further substantive rules needed for on-line transactions that provide safeguards and safe harbors against inadvertent assent and attribution.

Non-variable Rules UCITA contains a limited number of non-variable provisions listed in Section 113 to provide against abuses.

{5} All interested groups participated in UCITA's drafting process. Most support UCITA as a reasonable accommodation and consensus (see the attached listing of both large and small licensees and licensors.) Some based their concerns on their view that more mandatory rules should exist; that government should intervene to establish the terms of the contract rather than the marketplace. In short, they would go further than Section 113 and impose for every transaction rules, which many view would hamper innovation and new technologies that currently cannot be fully envisioned.

## CURRENT LAW

{6} Tangible product transactions form the foundation of our current statutory and common law. Current law is not designed to be applicable to intangibles and information. Both licensors and licensees of software and information products are looking for clear, consistent rules for the Information Highway. UCITA provides uniform rules essential for the global economy evolving in the Information Age.

{7} From the beginning of our Republic, the established business practices licensed intellectual property. Patents have been licensed since the Constitution was written; trade secrets licensed since the beginning of the Industrial Revolution; movies licensed to theaters since the beginning of the last century; and software licensed since it was invented. UCITA accepts this established business practice of licensing of intellectual property.

{8} Federal patent and copyright laws largely established intellectual property (IP) rights. States also establish IP rights under trade secrets and other laws. UCITA does not change or modify these federal and state law IP rights. Both patent and copyright cases routinely hold that state contract law governs contract law issues related to their subject matter.

{9} Under current common law, no implied warranties exist. Only statutory law establishes such warranties. For the first time, UCITA establishes implied warranties of merchantability and fitness for computer information, as well as for integration and informational content.

{10} Court decisions, since 1993, have enforced shrinkwrap and clickwrap licenses. UCITA places substantial limits on such licenses that protect the other party to the agreement.

{11} Under current law, software and information can be recovered by electronic means if there is no trespass or breach of the peace. Thus, in the event of a material default by the licensee, current common law places no restraint on electronic self-help practices. UCITA, however, does not permit electronic self-help unless the licensee separately negotiates and assents to it; and UCITA also imposes very substantial due process and other limitations on its use.

{12} Current common law and case decisions permit entering into inadvertent contracts electronically. UCITA changes the current common law and case decisions by imposing substantial safeguards to avoid inadvertent assent.

{13} UCITA also provides that consumer protection statutes and rules trump UCITA and any terms in a contract under UCITA. In addition, UCITA includes new statutory protections for consumers.

{14} UCITA provides certainty and consistency in the law that fosters the opportunity for this new information age to reach its full potential.

## I. THE NEED FOR UNIFORMITY

{15} Few question the need for uniform rules. Everyone who has actively studied the issue concludes that uniform rules are required. Those uniform rules can either be achieved by uniform state laws, where contract law has traditionally resided, or by federal preemption. Congress has a number of bills now before it that would preempt parts of state contract law. Most states also are seeing more ad hoc bills on e-commerce.

{16} In the early 90's a federal task force on intellectual property in the National Information Infrastructure (NII) concluded: "[the] challenge for commercial law is to adapt to the reality of the NII by providing clear guidance as to the rights and responsibilities of those using the NII. Without certainty in electronic contracting, the NII will not fulfill its commercial potential." [3]

{17} The White House issued a paper on July 1, 1997, that found: "Many businesses and consumers are still wary of conducting extensive business over the Internet because of a lack of a predictable legal environment governing transactions." [4]

{18} The White House Report notes the work of NCCUSL and states: "The Administration supports the prompt consideration of [the uniform state law] proposals, and the adoption of uniform legislation by all states." [5]

{19}The Department of Commerce reaffirmed statements made in the White House Paper: "It is important that governments set policies that facilitate, not hinder, Internet development."<sup>[6]</sup>

{20}The Conference Communiqué for Global Business Dialogue on Electronic Commerce (GBDe)<sup>[7]</sup> states:

We came together today for this inaugural conference of the GBDe in order to express our collective sense of urgency with respect to addressing electronic commerce issues by businesses and public authorities worldwide . . . .

It is the consensus position of the GBDe that inconsistent local, national and international patchwork regulation and inflexible regulatory constraints will deprive consumers of the economic benefits of an innovative electronic marketplace and would lead to significant uncertainty to consumers. Governments, administrations, parliaments and international organizations around the world are beginning to question the applicability of traditional, national legislative approaches to this new medium, which is uniquely swift and borderless. They are challenging us to develop effective self-regulatory and market-driven mechanisms that are not limited to national border, to address critical policy issues . . . .

We have drawn up proposals and criteria that will create a practical and flexible where needed legal and effective market-driven framework for the Internet and electronic commerce, a framework that promotes an open and frictionless global marketplace. Existing barriers must be overcome. In that process, we give precedence to effective self-regulation and technological solutions, wherever possible. In special cases, where regulation may be considered essential, any intervention of public authorities should be narrowly tailored, internationally-oriented, transparent and aiming at a level playing field.<sup>[8]</sup>

{21}At an American Law Institute meeting, Hal Burman, Office of Legal Advisor, Department of State, emphasized the great importance of a consistent U.S. legal framework to ensure success in international negotiations:

Our ability to extend and protect United States interests in a globalized economy and electronic commerce is the epitome of that globalized economy depends entirely on our ability to proceed from a basis of some commonality in state law. If there is any substantial delay [in completing UCITA] that will impair our effort, other countries are going to take the lead.<sup>[9]</sup>

{22}Despite perceptions to the contrary, small entrepreneurs with innovative ideas comprise the bulk of the software industry because the Internet and new technologies enable them to enter the marketplace at low capital cost.<sup>[10]</sup> The low entry cost into the Internet also provides exciting opportunities for customers to access the marketplace in an organized and, in a most effective way, to enhance their marketplace and negotiating power.<sup>[11]</sup> These factors played an important role in the following articulation by the White House of the principles that should govern e-commerce both internationally and domestically:

The following principles should, to the extent possible, guide the drafting of rules governing global electronic commerce:

- parties should be free to order the contractual relationship between themselves as they see fit;
- rules should be technology-neutral (i.e., the rules should neither require nor assume a particular technology) and forward looking (i.e., the rules should not hinder the use or development of technologies in the future);
- existing rules should be modified and new rules should be adopted only as necessary or substantially desirable to support the use of electronic technologies; and
- the process should involve the high-tech commercial sector as well as businesses that have not yet moved online.

. . . . The U.S. should work closely with other nations to clarify applicable jurisdictional rules and to generally favor and enforce contract provisions that allow parties to select substantive rules governing liability.

. . . NCCUSL and the American Law Institute, working with the American Bar Association and other interest groups, are urged to continue their work to develop complementary domestic and international efforts.<sup>[12]</sup>

## II. TWO ROUTES TO UNIFORMITY

{23}The universal rules needed domestically as the basis for global rules can be established either by:

Federal preemption, or  
Uniform State rules

{24}Traditionally, state law supplied contract law. Indeed, there is no federal common law of contract. Thus, to date, there has been a strong reliance upon uniform state laws to update contract law for e-commerce.

{25}A strong argument was marshaled for federal preemption of wholesale funds transfers. However, the Federal Reserve Board and other interested parties chose to have UCC Article 4A to provide the appropriate rules, which various states promptly enacted and incorporated into the federal rules for Fedwire, the CHIPS rules for international payments; and NACHA for automated clearing house rules.

{26}Similarly, Congress, while granting the Securities Exchange Commission (SEC) to exercise rule-making authority, permitted the consideration and enactment of revised UCC Article 8 as the vehicle to provide appropriate uniform rules for electronic holding and transfer of indirect securities holdings.

{27}The E-Sign federal legislation lifts the federal preemption on electronic signatures and records if a state enacts the Uniform Electronic Transactions Act (UETA). Twenty-three states have done so.

{28}Uniform state laws integrate E-Sign into the fabric of existing state contract law and the Uniform Commercial Code enacted by all 50 states. Significant contract questions are answered that would otherwise have to evolve from a developing federal common law of contracts.

{29}A shift to federal preemption also would move contract law cases to federal courts from the state courts which would require substantial reallocation of resources.

## **UCITA**

{30}NCCUSL promulgated the Uniform Computer Information Transactions Act (UCITA) in 1999; but UCITA was not fully styled for introduction until December of that year. UCITA covers:

- Software contracts and licenses
- On-line access to databases
- Contracts to distribute information over the Internet
- Contracts to create computer programs

{31}UCITA has been introduced so far in the following states: Arizona, Delaware, District of Columbia, Hawaii, Illinois, Maryland, New Jersey, Oklahoma, Oregon and Virginia.

{32}UCITA has been adopted in Virginia (House: 92-5; Senate: 39-0) and signed by the Governor. JCOTS studied UCITA again in depth during the summer and fall of 2000, holding extensive public hearing, considering many amendments, and recommending certain amendments which are discussed further below.

{33}In Maryland, the Governor signed UCITA into law, which became effective on October 1, 2000. The Speaker and President of the Senate were principal Patrons of the UCITA Bills. It was passed in the Senate 37-8 and in the House 96-39. The Bar Association of Delaware and the Chamber of Commerce have endorsed UCITA.

## **2001 AMENDMENTS TO VIRGINIA UCITA**

{34}The transformation of our national, indeed global, economy to the Information Age is as monumental as that of the Industrial Revolution, which transformed the U.S. from an agricultural to a machine-age economy. The rapid change now occurring with the Information Age offers grand opportunities for efficiencies, productivity, and a wealth of information immediately accessible in an organized and easily manipulated manner.

{35}As with any change substantially affecting the way we conduct business and value assets, one would expect reservations, concerns and differing perceptions. Thus, formulating consensus has been particularly challenging as some will always view change parochially without the give and take essential to achieving the larger public interest. Things are not going to be as they used to be, but with foresight and the full realization of the potential of the new technologies, the future is bright and promising.

{36}The Virginia Amendments undertake to address some of these concerns that include those of libraries, retailers, consumers, and users of information products. The Amendments set forth in H.B. 2412 passed the House of Delegates by a vote of 90-0 on January 31, 2001, and the Senate by a vote of 38:0 on February 8, 2001.

{37}H.B. 2412 is attached for your information. S.B. 1017 is a related Bill which makes certain amendments to Virginia's Consumer Protection to assure coverage of licenses and computer information. The principal and substantive changes made by H.B. 2412 are as follows:

{38}**Electronic Self-Help** As previously discussed, common law permitted electronic self-help (to disable software in the event of material breach). UCITA imposes substantial limitations: clear separate assent and negotiation of the term; and due process and notice provisions allowing disabling only in the most egregious cases of misappropriation. The H.B. 2412 amendments further clarify and expand these limitations by:

- Defining "wrongful use"
- Emphasizing that "separate assent" is truly to be separate
- Clarifying the intent of subsection (i)

{39}**Automatic (passive) restraints**: An automatic restraint definition is clarified, preventing use contrary to the contract while still

enabling use as permitted by the contract. Also, the amendment clarifies that a passive restraint cannot be employed as a remedy for a breach, which is covered by Section 59.1-508.16.<sup>[13]</sup> Any loophole, that might have been construed to be present, is closed.<sup>[14]</sup>

{40}**Consumer Protections** The intent of UCITA is that consumer protections trump contract provisions. The amendment to Section 59.1-501.5 clarifies that any (every) consumer protection law, including but not limited to the Virginia Consumer Protection Act, trumps.<sup>[15]</sup> S.B. 1017 amends the Virginia Consumer Protection Act to make it clearly applicable to licenses and computer information.<sup>[16]</sup> Another amendment requires mass-market (consumer) licenses to "expressly and conspicuously" set forth any designation of an exclusive forum.<sup>[17]</sup> In a mass-market (consumer) license, the term must be available before assent and after assent in a form readable by the licensee.<sup>[18]</sup>

{41}**Transferability** In a sale or acquisition of an affiliate or subsidiary, UCITA allows transferability to preserve the integrity of information or compatibility of processing systems.<sup>[19]</sup>

{42}**Libraries** In discussions with the Virginia libraries, a new section is included that partially resolves concerns. As a default rule, unless the parties otherwise agree, with respect to a tangible copy (e.g. CD-ROM) a non-profit library, archive or educational institution may subject to the limitations and restrictions of copyright law

- lend that copy to users in the ordinary practices of non-profit libraries or archives
- make a copy for archival or preservation purposes
- engage in inter-library lending
- make classroom and instructional use of a tangible copy.<sup>[20]</sup>

However, the default rules can be varied if the change is conspicuous and specifically assented to.<sup>[21]</sup> Further, if the term is not provided in advance, the institution must know or have reason to know it will be provided later with a cost-free return if it rejects the term.<sup>[22]</sup> These provisions do not apply to an on-line transaction.<sup>[23]</sup> Further, the amendment makes clear that unenforceability of a term contrary to fundamental public policy including those under federal copyright law continues fully to apply.<sup>[24]</sup> With some reservations, the Virginia Library Association, with this amendment, dropped its opposition to the implementation of UCITA in Virginia.

{43}**Service Providers** Amendments are included that make clear that to the extent telecommunications companies are regulated, or are merely a conduit, they are not within the scope of UCITA.<sup>[25]</sup>

{44}**Motion Pictures** While contracts to create motion picture and theater distributions are excluded, an amendment includes mass-market transactions for movies (e.g., over Internet or cable TV).<sup>[26]</sup>

## **B. UCITA THEMES**

### **1. Freedom of Contract**

{45}UCITA, like the UCC is premised on the parties having freedom of choice. The terms and effect of a contract are determined by agreement rather than by legislative fiat. The exercise of contract choice opens up full opportunities for innovation and growth. With certain limited exceptions the terms expressed by the parties in their agreement control.<sup>[27]</sup> If their agreement is silent, then trade usage and the parties; course of dealing and performance are looked to, and only if the contract is both silent and trade usage and course of performance is unhelpful, do the "gap-filler" provisions of UCITA apply.<sup>[28]</sup>

### **2. Information and First Amendment**

{46}Other law, such as patent and copyright law, establishes rights in intellectual property. UCITA specifically provides that federal preemption applies.<sup>[29]</sup> State intellectual property law supplements UCITA and is not displaced by UCITA.<sup>[30]</sup> UCITA adopts a neutral position with respect to what, ultimately, are issues of federal and international information rights policy. However, UCITA provides a basis for case by case resolution of the myriad issues in Section 105(b).<sup>[31]</sup>

### **3. Fundamental Public Policy Issues**

{47}A principal concern of consumers and other users and developers of computer information has been that the contracts, which provide for its use, should not contain provisions which violate fundamental public policies. The Drafting Committee did not want to depart from the longstanding policy that a statute premised on freedom of contract should not be a regulatory statute, and thus was reluctant to include in the statute a laundry list of impermissible terms. Instead, members of the Drafting Committee worked with members of the academic community for several months to craft a solution which would recognize the legal principle that certain terms of certain contracts may be unenforceable because they violate a fundamental public policy. That solution is now embodied in Section 105(b) and its accompanying comments.<sup>[32]</sup>

## **C. SCOPE**

### **1. Limited to "Computer Information Transactions" (Section 103 (a)).**

{48}UCITA covers 'computer information transactions', i.e. 'an agreement' to create, modify, transfer, or license computer information or

informational rights in computer information.[33] UCITA applies to contracts to license or buy software, contracts to create computer programs, contracts for on-line access to databases and contracts to distribute information over the Internet. UCITA does not apply to goods such as television sets, stereo equipment, airplanes or traditional books and publications. Goods generally remain subject to UCC Article 2 or Article 2A.

## **2. Opting in and Opting Out (Section 104)**

{49}Under common law, the right of parties to choose generally permits them to adopt the law they may wish to apply to their transaction. However, UCITA places some specific restrictions on opting in or out in order to safeguard the parties.[34]

## **3. Exclusions from UCITA**

{50}UCITA does not affect transactions in the core businesses of other information industries (e.g. print, motion picture, broadcast, sound recordings) whose commercial practices in their traditional businesses differ from those in the computer software industry. UCITA expressly excludes:

- a. Financial services transactions;[35]
- b. Motion pictures, broadcast and cable TV, other than mass-market transactions in computer information;[36]
- c. Sound recordings, musical works, phonorecord or enhanced sound recording;[37]
- d. Compulsory licenses;[38]
- e. Contracts of employment of an individual, other than as an independent contractor, and news gathering persons;[39]
- f. A contract which does not require that the information be furnished as computer information or in which the form of the information as computer information is otherwise *de minimis* with respect to the primary subject matter of the transaction;[40]
- g. Newspapers, magazines, books, and other print forms by the definition of 'computer information' except when transferred in electronic form (e.g. over Internet by license),[41] and
- h. E-mail communications merely about the agreement.[42]

## **E. ASSENT: UCITA'S SAFEGUARDS AGAINST INADVERTENT ASSENT AND SAFE HARBORS FOR CONTRACT FORMATION**

{51}There are a number of concepts in UCITA that need to be read together to fully appreciate the safeguards incorporated to protect the parties from inadvertent contracts, and place substantial limitations on clickwrap licenses, particularly in e-commerce. Some of these protections do not exist in common law. These concepts include:

1. Opportunity to Review: Before conduct can be assent above, there must be an opportunity to review the terms.[43]
2. 'Authenticate': Section 102(6) includes 'signature' but also includes "with the intent to sign a record, otherwise to execute or adopt an electronic symbol, sound or process referring to, attached to, included in, or logically associated or linked with, a record or term." [44] There is no authentication without an intent for the authentication to be a signing. The other alternative in common law and UCITA is manifesting assent by contract.
3. Agreement by conduct: "intentionally engages in conduct or makes statements with reason to know that the other party or its electronic agent may infer from the conduct or statement that the person assents to the record or term";[45]

-there must be 'intent' and also "reason to know" to be proven from all the circumstances

-if a party denies assent, "intent" or "reason to know" must be proven with the "burden of persuasion" on the party assenting the contract.

-the circumstances may include a "reconfirmation" as a safe harbor, i.e. an initial click on "I agree" followed by a second display asking whether the person really intends to agree to the agreement displayed and a second click in response thereto.[46]

The "reconfirmation" is not ordinarily employed or required today. UCITA adds this safeguard, which will change existing business practice.

4. Later terms are effective only as follows:

-after beginning performance or use, later terms are adopted only "if the parties had reason to know that their agreement would be represented by a later record to be agreed upon." [47]

-if the parties did not have reason to know of later terms, the later terms are proposed modifications.[48]

-if the parties did have reason to know that would be proposed for assent, if agreed to the later terms are part of contract, if not agreed to the transaction is unwound.[49]

-if one party is to supply terms later, Sections 304 and 305 apply.[50]

5. In a Mass-market License, the licensee is entitled to reject the contract with later terms for any reason and obtain not only a refund but incidental costs of return or destruction and reasonable and foreseeable costs of restoring the licensee's system;[51]

6. Pre-transaction Disclosure: Section 211 provides a strong incentive for disclosure of all terms before the licensee must pay or gets delivery, and lastly;<sup>[52]</sup>

7. 'Attribution' to the party to be bound is required. The efficacy of an attribution procedure is determined by the circumstances including any agreement of the parties.<sup>[53]</sup> Commercial reasonableness of an attribution procedure is a factor in making that determination.<sup>[54]</sup>

In short, a party to be bound must have an opportunity to review the terms, then assent with an intent to authenticate (sign) or intend with his conduct to agree and have reason to know that the other party will infer assent; (or if the opportunity to assent is after performance or use, the party to be bound must have reason to know there are later terms and assent, and in a mass-market transaction the party can return the item with a cost-free refund), and lastly, the claimant carries the burden of establishing attribution.<sup>[55]</sup>

## **E. ELECTRONIC CONTRACT (SECTIONS 212-215)**

{52}A record or authentication may not be denied legal effect, validity or enforceability solely on the ground that it is electronic.<sup>[56]</sup> A group of sections then set forth particular rules to be used when an electronic record or authentication is at issue.

## **F. WARRANTIES (PART 4)**

{53}UCITA provides the following basic warranties, which will be familiar to practitioners not found in common law but provided statutorily by UCITA: quiet enjoyment and non-infringement, merchantability of a computer program, information content and fitness for licensee's purpose and system integration. It also clarifies what is an express warranty. UCITA delineates the manner in which implied warranties may be disclaimed. Implied warranties are not generally recognized and/or clear under common law. UCITA thus significantly extends warranties over those imposed under current law.

### **1. Implied Warranty, Informational Content**<sup>[57]</sup>

{54}UCITA establishes a new implied warranty which focuses on the accuracy of data provided under a contract. The basic warranty states: "a merchant that, in a special relationship of reliance with a licensee, collects, compiles, processes, provides or transmits informational content warrants to its licensee that there is no inaccuracy in the informational content caused by the merchant's failure to perform with reasonable care."<sup>[58]</sup> Note that this warranty does not guarantee that there will be no inaccuracies caused by a failure to use reasonable care.

### **2. Implied Warranty, Licensee's Purpose; System Integration**<sup>[59]</sup>

{55}If licensor has reason to know of any particular purpose for which the information is required that the licensee is relying on the licensor for expertise, there is an implied warranty that the information will be fit for that purpose. The implied warranty of fitness for a particular purpose does not arise if, from all the circumstances, it appears that licensor was to be paid for the amount of its time or effort regardless of the suitability of the information. In this scenario, the implied warranty is that there is no failure to achieve the licensee's particular purpose caused by the licensor's lack of reasonable care and workmanlike effort to achieve that purpose.

## **G. TRANSFER OF INTERESTS AND RIGHTS (PART 5)**<sup>[60]</sup>

{56}UCITA generally presumes that transfer can be made of a contractual interest under a license.<sup>[61]</sup> However, transfer may be prohibited under other law (e.g. copyright law), or may not be allowed if such a transfer would materially change the duty of the other party, materially increase the burden or risk imposed on the other party, or materially impair the other party's property or its likelihood or expectation of obtaining return performance.<sup>[62]</sup>

{57}However, if the parties agree to a term prohibiting transfer, that term is enforceable.<sup>[63]</sup> In a mass-market license, the term must also be conspicuous.<sup>[64]</sup>

## **H. FINANCING ARRANGEMENTS**<sup>[65]</sup>

{58}UCITA establishes bridge rules for license financing transactions that are not governed by UCC Article 9. UCITA describes two such transactions:

- Financing relationships where the financier (e.g. a person who makes a financial accommodation but is neither the licensor nor a secured party under Article 9) does not become a party to the license; and
- Financing relationships where the financier becomes a "conduit" party to the license and passed through the rights to the ultimate licensee (this is akin to a finance lease under UCC Article 2A).<sup>[66]</sup>

{59}In transactions where the financier does not become a party to the license, the financier receives neither the benefits nor the burdens of the license, but is permitted to separately contract for additional conditions on the licensee's right to use the licensed information. For example, under Section 509, unless the licensee is a consumer, a term between the financier and the licensee that the licensee's obligations are irrevocable and independent is enforceable.<sup>[67]</sup> Note that in all such cases, the licensee is contracting away its own right to act, but not

conveying any part of the license itself.

{60}For a "finance license," there are different rules: (1) it must be permitted under Section 503, since it technically is a transfer; (2) clear notice must be given to the licensor; and (3) the licensee basically must look to the licensor for its rights and obligations, and not to the finance licensor, but the licensee remains subject to any additional conditions placed on it by the terms of the financial accommodation contract.[68]

{61}If a licensee materially breaches a financial accommodation contract, the financier may cancel the contract and pursue its remedies subject to the following restrictions: (1) if the financier became a licensee and made a transfer that was effective under Section 508, then it is entitled to exercise the remedies of a licensor, including rights granted under Section 815, which are subject to Section 815's limitations; [69] (2) if the financier did not become a licensee, it may enforce a contractual right to preclude the licensee's further use of the information but otherwise has no rights to the information of the license; [70] and (3) even if the financier has a contractual right against the licensee to take possession of the information, or have the license transferred to the financier, this right must comply with the transfer rules of UCITA or it will not be effective. A financier's remedies always are subject to the rights of the licensor.

## **I. REMEDIES: LIMITATIONS ON ELECTRONIC SELF-HELP**[71]

{62}UCITA's default rule prohibits electronic self-help.

Current law, without UCITA, permits self-help if there is no trespass or breach of peace. Some cases do require some notice of the provision in the contract.

UCITA permits the parties to agree to a provision for self-help; but even a self-help provision, is prohibited if its exercise will result in substantial harm to the public health and safety or grave harm to the public interest. A term to permit self-help is not valid unless the license has a separately-assented-to term that allows a limited exercise of electronic self-help. If authorized, before exercise, 15-day notice must be given to the person, place and in the manner designated by the licensee. Wrongful exercise results in consequential damages. Expedited injunctive relief is mandated.[72]

These UCITA provisions, when taken together with the provisions of Section 815, are so restrictive that it is unlikely that any licensor will be able to effectively use electronic self-help except in the most egregious cases; e.g. where a licensee is improperly disclosing the licensor's confidential and proprietary information. Most licensors would not agree to negotiate such provisions into their standard form contracts; thus it is a major benefit for licensees that UCITA effectively excludes electronic self-help from standard form contracts. UCITA expressly prohibits electronic self-help in mass-market transactions.

### **2001 Virginia Amendments**

{63}As stated above, the 2001 Amendments further strengthen and clarify these substantial limitations and restrictions on electronic self-help.

## **J. CONSUMER PROTECTIONS ARE PRESERVED AND MANDATED**

{64}While many of the transactions to be covered by UCITA are commercial between merchants, UCITA also extends consumer protections to UCITA transactions.

Section 105(c) explicitly provides:

(c) Except as provided in Subsection (d), if this [Act] or a term of a contract under this [Act] conflicts with a consumer protection statute [or administrative rule], the consumer protection statute [or rule] governs.

{65}Subsection (d) sets forth rules that enable e-commerce by allowing an electronic record, authentication, and conspicuousness. The Official Comments clearly state that "timing, manner and content" of disclosures are unmodified by those e-commerce rules. However, to the extent a state provides for a "writing" and does not wish an electronic message to be authorized, a legislative note instructs the state to except such statutory provisions.

{66}UCITA's objective is to have all consumer protections extend to computer information transactions. If amendments to existing state laws are needed, the drafters encourage them to be made to accomplish application of such consumer protections regardless of whether paper or electronic, or the subject of the transaction. Virginia has done that in S.B. 1017.

{67}UCITA: (1) retains existing consumer protection laws, (2) adopts consumer rules in Article 2, and (3) adds limited additional protections appropriate for issues associated with computer information transactions.

{68}Many contract law rules in UCITA benefit consumers. The doctrines of unconscionability, good faith, and fundamental public policy provide important consumer protections. But these rules also affect more than consumer transactions and respond to commercial concerns as well. So do the rules in UCITA (like those in Article 2) that disclaimer of implied warranties in a record must be conspicuous, or the rule in UCITA that a contractual choice of forum is unenforceable if it is unreasonable or unjust, or the rule in UCITA that assent is not effective unless there was an opportunity to review terms prior to giving assent. All of these and other rules benefit consumers but are not typically

denominated as 'consumer protections' rules. They contribute to the fact that UCITA creates a world in which consumers are better off than under current law.

{69}UCITA also includes rules focusing solely on consumer contracts and rules focused on mass-market contracts, which include all consumer contracts.

Section 105(c) provides that, except for stated rules regarding electronic commerce, if there is a conflict between UCITA and a consumer protection statute, the consumer protection law governs. Consistent with this theme, UCITA enacts rules preserving existing consumer law even if that result would not necessarily occur under other state law, such as:

Section 104: an agreement to opt into or out of UCITA cannot change a mandatory consumer protection law that would otherwise apply,

Section 109(a): an agreed choice of law cannot alter an otherwise applicable consumer protection rule that cannot be varied by agreement.

{70}UCITA retains consumer protection rules contained in UCC Article 2 including:

Section 303: a contract term requiring that modifications of contract be in writing is not enforceable in a consumer contract unless the consumer manifests assent to the term,

Section 704: licensee has a right to refuse tender of a copy that does not perfectly conform to the contract,

Section 803: consequential damages for personal injury cannot be disclaimed for a computer program contained in consumer goods.

{71}UCITA establishes various consumer protection rules focused on computer information transactions that do not exist under current law. These include:

Section 104: a term changing the application of UCITA to the transaction must be conspicuous in a mass market license,

Section 209: a license cannot alter terms expressly agreed between the parties and, if presented after delivery, the licensee has a cost-free right of return if it refuses terms,

Section 214: a consumer has a right to avoid an online contract if it acts promptly to avoid the effect of an electronic mistake,

Section 304: safe harbor rule for changing terms in a continuing contract requires that the licensee that is a consumer be given a right to terminate when a change is made,

Section 409(b): a warranty to a consumer extends to all individual consumers in the family or household if the use should have been expected by the licensor,

Section 503: a term that prohibits transfer of a contract right must be conspicuous for a mass market transaction,

Section 805: the statute of limitations for consumers cannot be reduced by agreement.

## **K. CHOICE OF LAW AND FORUM**

{72}UCITA is an e-commerce statute in which transactions are:

global  
borderless  
faceless

{73}Absent authorization for choice of law and forum, parties to a license (contract) would be subject to, and have to attempt to comply with the laws of every country in the world and that of each state. Knowing and applying laws of 190 countries would be impossible for small business and expensive to major enterprises. Particularly for small-business licensors that provide competition and innovation, the cost would be prohibitive. E-commerce laws have allowed choice.

{74}UCC Articles 4A, for e-commerce funds transfers, and Revised Article 5, for electronic letters of credit, likewise recognized the necessity in such a global environment, with comprehensive choice of law and forum provisions as follows:

4A-507 "The law of a jurisdiction selected [by the parties] may govern, whether or not that law bears a reasonable relation to the matter in issue." [73]

5-116(a) "The jurisdiction whose law is chosen [by the parties] need not bear any relation to the transaction." [74]

5-116(e) "The forum for settling disputes may be chosen in the manner and with the binding effect that governing law may be chosen in accordance with subsection (a)" [75]

(2) UCC Article 1 is currently under revision and the current draft changes provide:

1-301(a) "An agreement by parties to a transaction that any or all of their rights and obligations are to be determined by the law of this state or of another state or country is effective." [76]

{75}The Reporter's (Professor Neil Cohen of Brooklyn Law School) Notes state:

This recognition of party autonomy with respect to governing law has already been established in several Articles of the Uniform Commercial Code (See UCC Section 4A-507, 5-116 and 8-110) and is consistent with international norms. See, e.g., Inter-American Convention on the Law Applicable to International Contracts, Article 7 (Mexico City, 1994); Convention on Law Applicable to Contracts for International Sale of Goods, Article 7(1) (The Hague 1986); E.C. Convention of Law Applicable to Contractual Obligations, Article 3(1) (Rome 1980)[77]

Under UCITA, choice of law cannot alter applicable consumer protection law. Choice of forum cannot be "unjust and unreasonable" (amended by Virginia to read "or") which is current federal and predominant state law.

{76} Virginia UCITA also requires a term for an exclusive forum in a mass-market transaction to be conspicuous.

## **L. COPYRIGHT LAW -- Libraries: Quest for Change in Copyright Law**

{77} The libraries, through their associations and the Digital Futures Coalition, have focused their concern primarily on issues related to the Copyright Law, that are the same concerns for which they have been lobbying Congress for changes in the Copyright Law.

{78} The dramatic transformation from books to digital technology over the last two decades has had an exciting but challenging impact on the speed and availability of information. A book can be used by only one person at a time; a digital record can be simultaneously available to thousands, 24 hours a day, anywhere.

{79} As indicated in Section A above, the Virginia UCITA contains a default rule for tangible copies of digital products (such as CD-ROM) where a tangible book and a tangible CD-ROM have some parallels, and the guidance worked out cooperatively or in decisions make it more possible to have some objective understanding of the application of "fair use" and "first sale." However, downloading online without a tangible media enables instantaneous dissemination to thousands with substantial abuse possible. No parameters have been set by Congress, the Copyright Office, or the industries to define an appropriate application for online information products. The Copyright office has held a number of proceedings over the last two years and have not found evidence of abuses in licensing practices or a basis for establishing guidelines. UCITA's position has been that the appropriate forum to resolve the online issues is Congress and the Copyright Office. In that regard, the following points are relevant:

### **1. DIGITAL INFORMATION HAS BEEN AND WILL BE LICENSED WITH OR WITHOUT UCITA**

{80} Licensing of IP is as old as the Republic, and common for licensing of:

- o patents since the Constitution was adopted
- o trade secrets since the Constitution was adopted
- o movies and recordings-since invented
- o digital information since invented

· Digital information is currently licensed to libraries and will continue to be licensed with or without UCITA.

### **2. UCITA IS NEUTRAL ON SALE OR LICENSING AND DEFERS TO FEDERAL COPYRIGHT LAW**

{81} UCITA recognizes either sale or licensing of Intellectual Property (IP).

- UCITA specifically provides that federal law (e.g. Copyright Act) preempts UCITA and terms of contracts under UCITA (Section 105(a)).
- UCITA further provides that contract terms inconsistent with fundamental public policy (e.g. innovation, competition, free expression, fair use) are not enforceable (Section 105(b)).
- UCITA also makes unenforceable contract terms that are "unconscionable" (Section 111) or lacking in "fair dealing" (Sections 102(a)(32) and 114(b)).
- UCITA contains safeguards against inadvertent assent (Sections 112, 202, 208, 209, 212, and 213).
- These UCITA provisions are an advance over current common law for licensing.

### **3. CONGRESS AND THE COPYRIGHT OFFICE ARE THE APPROPRIATE FORUMS FOR CHANGES TO COPYRIGHT LAW**

{82} Congress has exclusive jurisdiction of copyright law and DMCA has authorized certain studies and proceedings to be conducted by the Copyright Office for distance education and exemptions.

- State legislatures do not have the expertise or constitutional authority to prescribe the "do's and don'ts" for licensing of digital information.

### **4. CONGRESS AND THE COPYRIGHT OFFICE HAVE BEEN CONSIDERING PROPOSALS FOR EXEMPTIONS AND CHANGES**

{83} Congress and the Copyright Office are the appropriate forums for changes to copyright law.

Fair Use is an imprecise doctrine that requires weighing of factors which requires examining facts and circumstances on a case-by-case basis.

#### **1. Legislative History of DMCA:**

{84}· The principle of fair use involves a balancing process, whereby the exclusive interests of copyright owners are balanced against the competing needs of users of information<sup>[78]</sup>

## 2. Report on Distance Education (May 1999)

{85}· "It [fair use defense] is flexible and technology neutral. It requires courts to examine all the facts and circumstances, weighting four non-exclusive statutory factors. While there are not yet cases addressing the application of fair use to digital distance education, a court's analysis will depend on elements such as subject matter of the course, the nature of the educational institution, the ways in which the instructor uses the material, and the kinds and amounts of material used."<sup>[79]</sup>

· "There is virtual unanimity that the doctrine of fair use is fully applicable to uses of copyrighted works in the digital environment, including in distance education" (at page xi).

· The Report urges:

§ "clarification in the legislative history including examples of digital use that qualify as fair use"

§ discussion of guidelines by interested groups

{86}The Report sees no need to abandon or regulate "the long-standing licensing system"<sup>[80]</sup>

§ "We have not otherwise seen sufficient evidence of a need for legislative solution moving away from the general free market approach of current law. At this point in time we recommend giving the market for licensing of non-exempted uses leeway to evolve and mature. Because the field of digital distance education is growing so quickly, and effective licensing and technologies may be on the horizon, we suggest revisiting the issue in a relative short period of time." (at page xxix).

## 3. Exemptions Final Rule<sup>[81]</sup>

{87}· "Licensing": Many of the complaints aired in this rulemaking actually related primarily to licensing practices."<sup>[82]</sup>

· "Commenters and witnesses who complained about licensing terms did not demonstrate that negotiating less restrictive licenses that would accommodate their need has been or will be prohibitively expensive or burdensome."<sup>[83]</sup>

· The record in this proceeding does not real that 'pay-per-use' business models have, thus far, created adverse impacts on the ability of users that would justify any exemptions from prohibitions or circumvention."<sup>[84]</sup>

· "7. 'Fair Use' Works A large number of commenters urged the Register recommend an exemption to circumvent access controls measures for fair use purposes the classes are scientific and social databases, textbooks, scholarly journals, academic monographs and treatises, law reports and educational audio/visual works."<sup>[85]</sup>

{88}"No evidence was submitted that specific works in these named classes have been or are likely to be inaccessible because educational institutions or libraries have been prevented from circumventing them."<sup>[86]</sup>

## 4. Summary

{89}· The dramatic transformation from books to digital technology over the last two decades has had an exciting but challenging impact on the speed and availability of information. A book can be used by only one person at a time; a digital record can be simultaneously available to thousands, 24 hours a day, anywhere.

· Both Congress and the libraries have struggled with how "fair use" applies to a digital record; the libraries have not been satisfied with what Congress has done to date.

· IP professors, writing to the Presiding Officers of the Maryland General Assembly, acknowledge that the matter is in the hands of Congress, and a case-by-case application of the Law: "[T]he U.S. Constitution may still preempt some of these license terms . . . . We believe that when this issue reaches the Supreme Court, the Court will conclude that federal law indeed does preempt . . . terms that interfere with fair use or override other statutory limitations on copyright protection . . . . The federal copyright law does not specify with particularity which terms may and may not be varied by contract; these decisions are made on a case-to-case basis by federal courts."

· Federal copyright law is not for States to change. UCITA specifically provides that whatever federal law preempts is preempted. What Copyright Law permits or prohibits is the prerogative of Congress. State contract law is not the place to change copyright law.

## CONCLUSION

{90}Virginia leads the nation in establishing uniform rules for the Information Age. The modern rules for choice of law and forum, and the UCITA rules that are embodied in The Virginia Act, provide a basis for parties to choose Virginia law for their transaction; thus increasing the attractiveness of Virginia as the place to locate one's New Age business.

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## ENDNOTES

[\*]. An experienced commercial law attorney, Carlyle Ring handles the negotiation and documentation of commercial agreements for the purchase and sale of goods and services, alliances and joint ventures with U.S. and international entities, the acquisition and sale of operating businesses, the preparation of standard terms and general business transactions for Ober, Kaler, Grimes and Shriver in

Washington, D.C. Mr. Ring has considerable experience in matters involving the Uniform Commercial Code and its application to a wide range of transactions. He served as president of the National Conference of Commissioners on Uniform State Laws (NCCUSL) from 1983-1985. He has chaired UCC drafting committees, including the UCC Article 4A committee in 1989, the UCC Revised Article 3-4 committee in 1990, the UCC Revised Article 5 committee in 1995, and the UCITA committee in 1999. Mr. Ring has served on the UCC Permanent Editorial Board since 1985.

[1]. James S. Gilmore, *Uniform State Contract Law Facilitates Information Revolution*, Legal Backgrounder, July 14, 2000, available at LEXIS, News Group File, Most Recent 60 Days.

[2]. See definition of 'Agreement' in U.C.C. § 1-201(3)(West 2001). See also VA . CODE ANN. § 59.1-501.2 (a)(4) (Michie 2000); UCITA § 101(4) (West 2001).

[3]. Information Infrastructure Task Force, *INTELLECTUAL PROPERTY AND THE NATIONAL INFORMATION INFRASTRUCTURE: THE REPORT OF THE WORKING GROUP ON INTELLECTUAL PROPERTY RIGHTS*, 58 (Sept. 1995) available at <http://www.uspto.gov/web/offices/com/doc/ipnii>.

[4]. See The White House Paper, *A Framework for Global Electronic Commerce* at <http://www.ecommerce.gov/framwrk.htm#Background> (last visited Sep. 26, 2001).

[5]. *Id.*

[6]. *Id.*

[7]. The GBDe held its first international meeting in September 1999 of 70 CEO's or Board members, 110 government officials and representatives of international multilateral organizations. Principal presenters and participants included Mozell Thompson, FTC; Sanford Lituach, The Walt Disney Co.; Richard Brown, EDS; Steve Case, AOL; Louis Gerstner, IBM; David House, Nortel; Lew Platt, Hewlett Packard; and Bert Roberts, MCIWorldCom.

[8]. Global Business Dialogue on Electronic Commerce (GBDE), *Conference Recommendations* (September 13, 1999), available at <http://www.gbde.org/ie/archive/recommendations.html> (last visited Oct. 7, 2001).

[9]. Proceeding of American Law Institute, May 1998, transcript, at 145-46.

[10]. FCC Chairman William E. Kennard, *Connecting the Globe: The Asia-Pacific Initiative*, Remarks Before the Confederation of Indian History, (Sep. 22, 2000), available at <http://www.fcc.gov/Speeches/Kennard/2001/spweek024.html> (last visited Sep. 26, 2001).

[11]. See Lorin Brennan, *The Public Policy of Information Licensing*, 36 HOUS. L. REV. 61, 108 n.288 (1999).

[12]. The White House Paper, *supra* note 2, at <http://www.ecommerce.gov/framwrk.htm#3%'UNIFORM%20COMMERCIAL%20CODE'%20FOR%20ELECTRONIC%20COMMERCE>.

[13]. VA . CODE ANN . § 59.1-508.16 (Michie 2000).

[14]. H.B. 2412, Gen. Assem., Spec. Sess. (Va. 2001) (codified at VA . CODE ANN. § 59.1-508.16 (Michie 2000)).

[15]. *Id.*

[16]. S.B. 1017, Gen. Assem., Spec. Sess. (Va. 2001) (enacted).

[17]. H.B. 2412, Gen. Assem., Spec. Sess. (Va. 2001) (codified at VA. CODE ANN. § 59.1-505.3(1)(D) (Michie 2000)).

[18]. *Id.* (codified at VA. CODE ANN. § 59.1-508.9 (Michie 2000)).

[19]. *Id.* (codified at VA. CODE ANN. § 59.1-501.2 (Michie 2000)).

[20]. *Id.* (codified at VA. CODE ANN. § 59.1-503.10(a) (Michie 2000)).

[21]. *Id.* (codified at VA. CODE ANN. § 59.1-503.10(b)(1)-(2) (Michie 2000)).

[22]. *Id.* (codified at VA. CODE ANN. § 59.1-503.10(b)(3) (Michie 2000)).

[23]. *Id.* (codified at VA. CODE ANN. § 59.1-503.10(c)(2) (Michie 2000)).

[24]. *Id.* (codified at VA. CODE ANN. § 59.1-503.10(c)(3) (Michie 2000)).

[25]. *Id.* (codified at VA. CODE ANN. § 59.1-501.3(d)(5)-(7) (Michie 2000)).

[26]. *Id.* (codified at VA. CODE ANN. § 59.1-501.3(d)(2)(A) (Michie 2000)).

[27]. *Id.* (codified at VA. CODE ANN. § 59.1-501.9 (Michie 2000) (stating that choices of law in a consumer contract are not enforceable if they alter a statute, administrative rule or regulation may not be altered under Virginia law).

[28]. *Id.* (codified at VA. CODE ANN. § 59.1-501.13(b) (Michie 2000)).

[29]. UCITA § 105(a) (2001).

[30]. *Id.* § 114(a).

[31]. *Id.* § 105(b).

[32]. *Id.* § 105(b).

[33]. *Id.* § 102(11).

[34]. *Id.* § 104.

[35]. *Id.* § 103(d)(1).

[36]. *Id.* § 103(d)(3)(A).

[37]. *Id.* § 103(d)(3)(B).

[38]. *Id.* § 103(d)(4).

[39]. *Id.* § 103(d)(5).

[40]. *Id.* § 103(d)(6).

[41]. *Id.* § 102(11).

[42]. *Id.*

[43]. *Id.* § 112(e).

[44]. *Id.* § 102(6).

[45]. UCITA § 112(a)(e) (2001). *See also* RESTATEMENT (SECOND) OF CONTRACTS § 19(2) (1981) ("The conduct of a party is not effective as a manifestation of his assent unless he intends to engage in the conduct and knows or has reason to know that the other party may infer from his conduct that he assents." *Id.*)

[46]. UCITA § 112(d) (2001).

[47]. *Id.* § 208.

[48]. *Id.* § 302.

[49]. *Id.* § 202(e).

[50]. *Id.* §§ 304, 305.

[51]. *Id.* § 209(b).

[52]. *Id.* § 211.

[53]. *Id.* § 213(c).

[54]. *Id.* § 212.

[55]. *Id.* § 213(a).

[56]. *Id.* § 107.

[57]. *Id.* § 404.

[58]. *Id.* § 404(a).

[59]. *Id.* § 405(a).

[60]. *Id.* § 501 et seq.

[61]. *Id.* § 501(a).

[62]. *Id.* § 503.

[63]. *Id.* § 503(2).

[64]. *Id.* § 503(4).

[65]. *Id.* §§ 507-511.

[66]. *Id.* § 507(1)-(2).

[67]. *Id.* § 509.

[68]. *Id.* § 508.

[69]. *Id.* § 510(3).

[70]. *Id.* § 510(4).

[71]. *Id.* § 816.

[72]. *Id.* § 816(c)-(g)

[73]. U.C.C. § 4A-507 (2001)

[74]. *Id.* § 5-116(a)

[75]. *Id.* § 5-116

[76]. U.C.C. § 1-301(a) (Proposed Official Draft, 2001)

[77]. Organization of American States Fifth Inter-American Specialized Conference on Private International Law: Inter-American Convention on the Law Applicable to International Contracts, Mar. 17, 1994, Mar. 17, 1994, art. 7, 33 I.L.M. 732, 734 (1994); Hague Conference on Private International Law Draft Convention on the Law Applicable to Contracts for the International Sale of Goods, Oct. 30, 1985, art. 7(1), 24 I.L.M. 1575 (1985); European Communities: Convention on the Law Applicable to Contractual Obligations, art. 3(1), 1980 O.J. (L 266; 19 I.L.M. 1492 (1980)).

[78]. H.R. Rep. No. 105-551, pt. 2, at 25 (1998).

[79]. Government Printing Office, REPORT ON COPYRIGHT AND DISTANCE EDUCATION (1999) (Report on Copyright and Distance Education, Executive Summary, page viii) (*copy on file with author*).

[80]. *Id.* at page xxiii.

[81]. Exemption to Prohibition on Circumvention of Copyright Protection Systems for Access Control Technologies, 65 Fed. Reg. 64556 (Oct. 27, 2000) (codified at 37 C.F.R. pt. 201).

[82]. *Id.* at page 644565.

[83]. *Id.* at page 644563.

[84]. *Id.* at page 644564.

[85]. *Id.* at page 644571.

[86]. *Id.* at page 644571.

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### **Related Browsing**